EUROPEAN INVESTOR SENTIMENT INDEX

Q3/2021

QUARTERLY SURVEY

October 19, 2021

VENIONAIRE CAPITAL

EUROPE'S FIRST INTRODUCTION TO ITS "NEW NORMAL" LEADS TO RECORD HIGH INVESTMENTS

Western economies are showing signs of recovery from the COVID-19 pandemic. Concerns related to mutation variants have decreased, as vaccination efforts prove to be relatively effective. The European "Economic Sentiment Indicator" (ESI) remained high throughout Q3 (Eurostat, 2021). However, a new global wave of concerns in the form of international supply chain bottlenecks has materialized. The current supply gap in some sectors has resulted in significantly higher energy and import/export costs.

The venture sentiment actual decreased compared to Q2 but remains very strong. The outlook for Q4 increased over the anticipated outlook for Q3 but is still significantly less optimistic than the observed actual. The trend of high investment activity and higher valuations of ventures continues and we see more emerging unicorns across several industries and geographical locations. On an yearly basis the market is performing strong, however we see a quarterly drop in investment volume.

"Optimistic market sentiment seems to fade. On the one hand we see large transactions, and a rising number of European unicorns throughout the European Union. On the other hand early-stage transactions become more difficult, as individual angel investors can't lift the sizeable seed rounds alone. Investment Networks and syndicates – such as European Super Angels Club – move into earlier rounds and replace individual investors. Having noticed this, current developments lead to inflated valuations, tighter terms and conditions and a higher ratio of declined investments – while more and more newly founded companies are entering the market. European and national policy for early-stage markets will need to tackle these effects, as innovation dynamics and top tier talent demand fruitful soil to develop in Europe."

Berthold Baurek-Karlic
CEO / founder Venionaire Capital

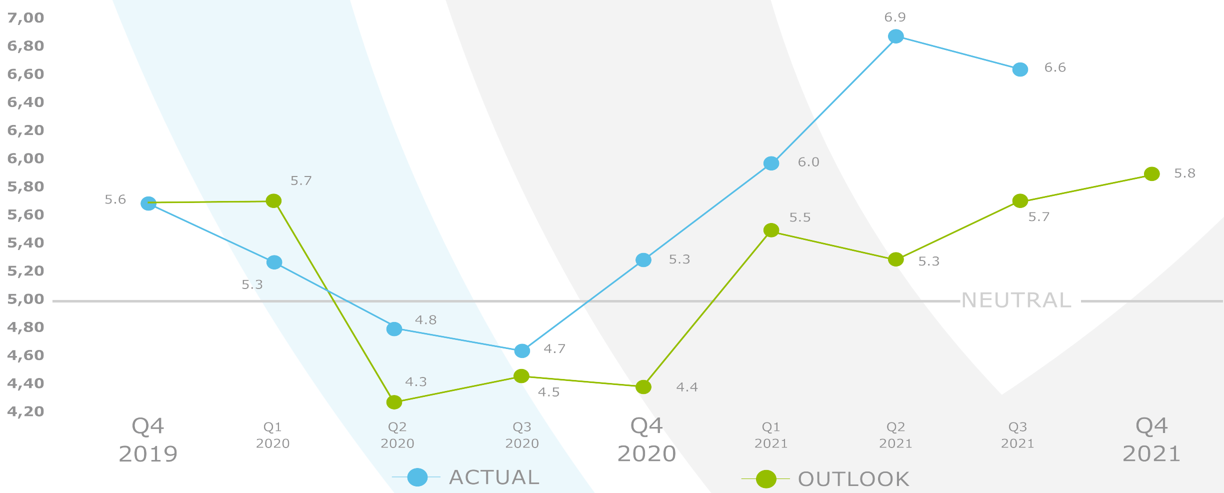
INDEX REMAIN IN POSITIVE TERRITORY. FIRST DROP IN QUARTERLY INVESTMENT VOLUME SINCE Q1 2020

For Q3 2021 we have recorded a decrease in the sentiment actual for the first time since Q3 2020. This is parallel to the first quarterly drop in investment volume since the beginning of the COVID-19 pandemic and Brexit in Q1 of 2020. This quarter's index actual stands at 6.65, which is still high in positive territory but constitutes a -3.12% drop over the previous quarter.

The gap between expectations and actual sentiment shrunk. Currently, we are observing a 12.0% difference compared to 29.6% last quarter. Uncertainty in the current economic situation still spills over investors' confidence about the near-term future, even though

Investment in European start-ups tracked at $24.2 billion in 1,590 deals in the year's third quarter. This represents a 13% volume decrease from the previous quarter, a record high of $30.6 billion in 1,821 deals. Nonetheless, this is a 140% increase compared to its year-over-year counterpart (CB Insights, 2021).

Global venture funding at all investment stages continued to grow in Q3 in terms of invested volume and number of deals. The United States and Asia lead the pack ahead of Europe in terms of volume and QoQ growth. Europe has continued to exhibit a record venture performance in 2021 with impressive YoY results and remains the third-largest venture region in Q3. However, the QoQ drop positions European venture funding to constitute only 17% of all global deals, the lowest proportion since Q2 2016. Compared with the development in the rest of the world, Q3 did not look too promising for the old continent.



Additionally, we observed another rather unexpected change. The UK, even after Brexit, set a new funding record of 7.7B in 453 deals while other European ecosystems shrank (CB Insights, 2021). Even though the French ecosystem had the spotlight in Q3 by raising the record sum of more than $1 billion in one day via three mega-rounds, some speculated that this is due to post-Brexit investment shifting from the UK to continental Europe (TechCrunch, 2021). This probably would impact the European sentiment next quarter, especially in terms of outlook, as some predictions pointed that the European start-up environment would depend more on the continent after Brexit.

Seed funding in Europe is reported to be $1.5 billion – a -27.3% decrease from the record-breaking $2.2 billion in Q2. Early-stage funding also decreased, but by just -3.85% from $7.8 billion in Q2 to $7.5 billion in Q3. The number of deals in seed and early stages dropped in Q3 parallel to the decrease in volume. Even late-stage funding suffered a significant QoQ reduction of -29.2%, falling from 26.7 billion in Q2 to 18.9 billion in Q3. The number of deals changed merely by one deal from 163 to 162 (Crunchbase, 2021). This suggests that valuations in the early stages might continue to be relatively high. This is also noticeable in the Venture Sentiment Index. In fact, valuations are the only component of the index that had a positive change of 0.22%, while all other variables turned negative to previous periods. Investors responded that they also anticipate valuations to continue to grow in Q4 with an index component change of 7.28%.

POSITIVE OUTLOOK FOR Q4, HIGH VALUATIONS, CHALLENGING DEAL ENVIRONMENT

Like the previous quarterly report, the outlook for Q4 2021 remains significantly below the actual sentiment for the completed quarter, while the outlook for the next quarter is up by 2.32% compared to the previous outlook for Q3 2021. Nonetheless, there is still a 12% discrepancy between the Q3 actual sentiment and the Q4 outlook. The high positive value of the observed index shows that the positive expectations for Q3 were justified. The difference could be explained by uncertainty deriving from COVID-19.

The decrease in the outlook for Q4 might be partially related to the current supply chain crisis, fuel and energy prices and microchips shortage on a global scale (Wang, Curran & Bloomberg, 2021). Furthermore, we think that the high valuation of start-ups plays an important part as well. Interviewed participants expressed their concerns about increasing valuations to inflate portfolio values and increase related risks. This can be reconfirmed with the findings reported in a sentiment survey by the EIF. They concluded that only 4% of participants expect their NAV to decrease in 2021 (24,6% in 2020). Simultaneously, 77% of participants believe that valuations will increase in 2022 while also stating that they think high company valuations are the most significant risk currently seen by VCs (Botsari, Kiefer, Lang & Legnani, 2021). Lastly, high valuations can result in a misleading sentiment if participants have not accounted for it while participating in the study.

In the Q2 report, we mentioned concerns regarding transitionary inflation. These concerns have become even tenser since the inflation might not be just transitionary but here to stay, as the Federal Reserve officials mentioned (Bartash, 2021). Global supply chain bottlenecks, higher cost of raw materials, rising energy prices and labour shortages should also be considered.

The most notable increase in the index stems from a 0.22% rise in investors' perception of start-up valuations in Q3. It must be noted that valuations' perception was also above neutral and growing since Q1 2021. All other factors in the index have decreased, with the sharpest move being the perception of the current fundraising environment decreasing by -7.56% from Q2. Another significant decrease is the decline in investors perception of deal flow quality which has dropped by 6.63% since Q2. It seems reasonable that there is an inverse connection between valuations perception and deal flow quality. These dynamics can be connected to the currently ongoing start-up hype in Europe with high valuations parallel to the ongoing uncertainty related to the COVID-19 pandemic.

FINTECH STAYS ON TOP, WHILE FOOD DELIVERY START-UPS WAGE WARS IN EUROPEAN CITIES

Globally, investing in FinTech is still as hot as before. While Q3 shows a slight decline in funding compared to Q2, it still more than doubles the amount of funding that FinTech companies received in 2020 (CBS Insights, 2021). While many news outlets reported that FinTechs in Europe and Latin America were booming in Q2, the third quarter shows the opposite. Europe and Latin America show the most significant decline in FinTech funding when compared to other regions globally. The second-largest European funding round for Q3 was for UK-based Revolut with a USD 800 million round valued at USD 33 billion. It should be noted that the global fintech funding is still higher than in the same quarter in previous years, so it will be interesting to see if this trend continues into Q4, meaning that Q2 of 2021 was a clear outlier in global FinTech funding.

FinTech is not the only sector that shows a decline in Q3. Global healthcare reached just half of the Q2 volume and the number of deals also decreased (CB Insights, 2021). However, as was the case with Fintech, on a YoY basis and until now, 2021 has been an extraordinary, record-breaking year for both sectors. It will be interesting to follow both sectors performance in Q4. Historically, the last quarter of the year tends to lag, but the trend was ceased in 2020.

Another sector is back on the leader boards once again: food & grocery delivery start-ups. After a cool-down phase following their 2019 mega-rounds, European delievery stratups hit record funding rounds. Examples can be the German Gorillas (USD 950M) and the Turkish Getir (USD 555M). These companies are operating at colossal losses in highly competitive markets fueled by a wide variety of funding, with investors hoping to own a share in the last fast delivery services standing at the end. Thus, it is no surprise that Gorillas raised the highest round in Europe with for its "war fund". Another delivery service called Picnic is not far behind, with a round of 705M USD raised with the Bill & Melinda Gates Foundation in the lead (Dealmatrix, 2021).

SUMMARY

The venture sentiment continues to be in positive territory. The outlook for Q4 is also positive, and the gap with the actual index seems to be closing. The positivity of the current quarter can be related to economies picking up speed after the pandemic. However, reported high valuations might be misleading for the ecosystem. There is still a general uncertainty surrounding the impact of COVID-19 and the development of inflation rates. Venture investment volume remained high compared to 2020. However, in this quarter post-Brexit UK continued to grow on a quarterly basis, while other European ecosystems did not manage to top their Q2 records. Lastly, fintech and healthtech attracted the most investment in Q3.

METHODOLOGY

Over fifty highly experienced investors (business angels, (corporate) venture fund managers and family offices) from 8 European countries were interviewed in September 2021 as part of the European Venture Sentiment Survey, conducted by Venionaire Capital. Venionaire Capital collects answers from a focus group in computer-assisted personal interviews and a much smaller control group to assess the indices based on a quarterly recurring survey. Those datasets are collected in two waves and finally merged. In both groups, Venionaire has aligned similar sets of investors, ranging from business angels to large corporate venture units as well as early- to later-stage venture capital funds from all over Europe (incl. Switzerland and the UK).

The indices for current sentiment and projected outlook are weighted indices, with emphasis on the ability/willingness of investors to invest, the perception of start-up valuations and the quality of deal flow.

COMPARABILITY

Sentiment surveys and indices are nothing new. They have been around for decades to quantify how a specific group of people feel about a market or economy. One of the most notable examples is the Consumer Confidence Index (CCI), which provides an indication of future consumption and saving of households. There are also surveys that focus on a specific market, or even an individual security. How can the results of these market sentiment surveys help market participants?

Let's look at the venture capital industry. This general economic information can greatly benefit both the investor and start-ups within a market. Investors can compare their own views and opinions to those of the general market or across different geographical regions and industry verticals. This will help them to adjust their investment behavior. Start-ups can use this information when growing their business internationally, when they prepare for fundraising or to slow down their business (return to bootstrapping – ahead of time) if the economic environment worsens. Market sentiment indicators are important for us in all industries and markets. Nevertheless, there is a limited number of market sentiment indices for the venture capital or start-up market available, which we found useful to work with.

Most indices available focus on a specific region, investors group or industry. Take EIF's VC Survey, which targets a highly professional group of regulated investors across Europe, but does not take accelerators or business angels into account. Our partners of Deutsche Börse Venture Network conducted a great report on market sentiment during the COVID-19 pandemic. It offers great insights, but it was a onetime publication.

We have developed our own "European Venture Sentiment Index", which shows in one simple number the general state of sentiment today and shows the current outlook in a second number.

THE EUROPEAN INVESTOR SENTIMENT INDEX

The index is based on feedback from different economic regions, as well as start-up sectors and reflects the general European Venture Sentiment. The methodology of the index was designed by Venionaire Capital in mid-2019. The project was led by its founder and managing partner, Berthold Baurek-Karlic, a serial entrepreneur and leading venture capital expert from Vienna, Austria. Berthold started his career in the statistics department of the Austrian Central Bank (OeNB).

"We attach great importance to providing our investors with an actual overview of the current investment climate in the European start-up sector. After this index has proven to be an important tool for our clients - including start-ups as well as investors - we have decided to make the results available to the public for the first time during the COVID-19 pandemic in the first quarter of 2020. Our aim was to draw public attention to the threatening situation of innovative young companies in Europe", explains Berthold Baurek-Karlic.

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Berthold Baurek-Karlic is the founder and managing director of Venionaire Capital, which specializes in M&A and venture capital. The Venionaire Group also includes the investment company MOTEC VENTURES (motec.vc) and the software provider DEALMATRIX (dealmatrix.com).

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As a passionate blogger (www.baurek-karlic.at), he writes regularly on various topics related to angel and venture investments, startups, and future technologies.

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David is responsible for the identification, screening, and evaluation of startups. Furthermore, David specializes in financial modelling; he supports Venionaire's clients with deal structuring, financial engineering and valuations. Before joining the team at Venionaire, he gained experience by accompanying a tyrolean startup in a leading position as Controller & Financial Analyst from early-stage through a Series A round up to a Share Deal exit. David has a Bachelor degree in Business Management & Entrepreneurship from the FHWien der WKW.

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Milan manages deal flow, analyses business models and prepares investment decisions. Prior to Venionaire, Milan gained professional experience as the first employee at a successful Dutch start-up as well as readying start-ups for investment at a Dutch angel network.

ABOUT

Venionaire is a entrepreneurial partner for investors, founders and institutionals. Our partners and team are specialized in venture capital and private equity investments, with an extensive track-record over more then a decade. We offer transaction and corporate advisory services – from due-diligence, valuation, deal structuring, (ghost) negotiating to alternative fund management – for investors, corporates, public entities and growth companies (startups / scaleups). Our track-record as entrepreneurs, advisors and investors shows deals in fields of corporate finance (M&A), (Corporate) venture capital, corporate startup engagement (CSE), digital transformation and high-tech innovation with a total volume of more than a billion Euros. In addition we serve as trusted partners for scouting, screening, technology-, market- and competitive analysis and valuation for bespoke investors and accelerators in Europe. We are proud of our performance within managed portfolios and increase our high-tech footprint everyday to support a future-proof economy.

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